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In the Supreme Court of the United States

OCTOBER TERM, 1966

No. ——

UNITED STATES, PETITIONER

v.

THE EQUITABLE LIFE ASSURANCE SOCIETY OF THE UNITED STATES

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

The Solicitor General, on behalf of the United States, petitions for a writ of certiorari to review the judgment of the United States Court of Claims in this case, entered on October 14, 1966.

OPINION BELOW

The opinion of the Court of Claims (App. A, *infra*, pp. 13–25) is reported at 366 F. 2d 967.

JURISDICTION

The judgment of the Court of Claims was entered on October 14, 1966 (App, A, *infra*, pp. 13, 51–52). On January 13, 1967, the Chief Justice extended the time for filing a petition for a writ of certiorari to and including March 13, 1967. We invoke the jurisdiction of this Court under 28 U.S.C. 1255(1).

STATUTES AND REGULATIONS INVOLVED

Sections 901 (a) and (b)(1) and 903 of the Internal Revenue Code of 1954, and Section 1.903–1 of the Treasury Regulations (1954 Code), are printed in App. B, *infra*, pp. 53–55.

QUESTION PRESENTED

The Internal Revenue Code of 1954 permits taxpayers to credit against their income tax any foreign income tax (§ 901(b)(1)) or "tax paid in lieu of a tax on income * * * otherwise generally imposed by" the foreign country (§ 903).[1] The question presented is whether taxes imposed by Canada and its provinces on the premiums received by life insurance companies are taxes "in lieu of" income taxes within the meaning of the latter provision.

STATEMENT

1. Respondent, a mutual life insurance company incorporated in New York State, conducted business in Canada and claimed credits against its federal income tax liability for taxes paid to the Dominion of Canada and the Province of Quebec in the years 1950 through 1955, and to the Province of Ontario in the years 1950, 1951, and 1952. The taxes in question were levied annually, at a rate of 2 percent, on the insurance premiums received from policyholders residing in the jurisdiction. Although the Dominion, Quebec and Ontario also levied income taxes, Equitable was

[1] The 1939 Code contains similar provisions (see § 131 (a) and (h)), which are applicable to some of the taxable years involved in this case.

exempt from them in respect of its life insurance business in Canada [2] (Fdgs. 2, 3, 7, 8–12, 15, 18, App. A, infra, pp. 26–29). The Court of Claims in this refund suit held that the premiums taxes were "in lieu of" the various Canadian income taxes within the meaning of Section 131(h) of the Internal Revenue Code of 1939 and Section 903 of the 1954 Code (App. B, *infra*, p. 54), and hence that Equitable was entitled to credit its premiums-tax payments against its federal income tax liability.

2. The tax systems of the three foreign jurisdictions may be briefly described as follows:

By the Excise Tax Act (II Revised Statutes of Canada (1952), c. 100) the Dominion imposes various excises, a manufacturers' sales tax, and other volume-of-business taxes. Section 4(1) of the Act imposed the 2 percent premiums tax involved in this case; by 1946 all insurance companies were taxed under this provision (Fdgs. 47–49, 51, 53, 59–60, App. A, *infra*, pp. 41–42, 43, 44, 46–48). The Dominion repealed the premiums tax as of 1957, whereupon the provinces—if they had not already done so—enacted the same tax (Fdgs. 66, 68, App. A, *infra*, pp. 49, 50). Section 30 of Part I of the Dominion's Income Tax Act (III Revised Statutes of 1952, c. 148) taxes life insurance companies on "the aggregate of the amounts credited to sharehold-

[2] In 1954 and 1955, Equitable paid a Dominion income tax under Part III of the Income Tax Act, III Revised Statutes of Canada, 1952, c. 148, §§ 106–110, which imposed a 15 percent tax on income received by nonresidents from Canadian investments (App. A, *infra*, p. 19, n. 1; Fdgs. 13, 15, 61, App. A, *infra*, pp. 28, 48).

ers' account or otherwise appropriated for or on account of shareholders during the year." Since foreign stock life insurance companies were by administrative ruling deemed not to have shareholders' accounts in Canada, and since mutual insurance companies have no shareholders, no such companies are subject to the tax. (Fdgs. 51–52, 64–65, App. A, *infra*, pp. 43–44, 49.)

As early as 1882, Quebec imposed annual taxes on major corporations, measured by paid-up capital and the number of places of business. Insurance companies paid those taxes until 1900, when a premiums tax was substituted. The tax rate for life insurance premiums was originally 1¾ percent; later it was raised to 2 percent. Quebec first imposed an income tax on corporations in 1932. It was in addition to the other taxes. After the Second World War and during the years involved in this case, Quebec imposed a 7 percent income tax on the net revenues of various corporations and businesses, which are also taxed by way of excises under other provisions of its Corporation Tax Act (Statutes of Quebec, 11 George VI (1947), c. 33). Insurance companies, among others, were not among the firms subject to the Act (see Section 6); they were therefore exempt from the income tax (Fdgs. 20–23, 67, App. A, *infra*, pp. 29–31, 49).[3]

[3] In 1957—after the taxable years at issue here—Quebec made its income-tax statute identical to the Dominion Income Tax Act so far as taxation of insurance companies was concerned (Fdg. 69, App. A, *infra*, p. 50).

In 1899, Ontario imposed an annual tax on various kinds of carriers, utilities, lending institutions, and insurance companies. The tax was generally measured by capital or equipment, but insurance companies were subject to a premiums tax instead, eventually at the rate of 2 percent for life insurance. The first income tax on corporations was enacted in 1932. During the years in issue here, Ontario, like Quebec, imposed a 7 percent income tax, pursuant to Section 14(1) of the Corporation Tax Act (Statutes of Ontario, 3 George VI (1939), c. 10: Revised Statutes of Ontario, 1950, c. 72), from which insurance companies, banks, railway companies, telephone companies and certain other companies were exempted (Fdgs. 24–27, App. A, *infra*, pp. 31–33).[4]

REASONS FOR GRANTING THE WRIT

1. The Court of Claims held in this case that Canadian taxes on the premiums of life insurance companies may be credited against federal income tax liability. Quite apart from the implications of this ruling for the general scope of the foreign tax credit (see below), it has a large direct impact upon the federal revenues. Existing claims of life insurance companies for income-tax refunds based on past payment of Canadian premiums taxes aggregate more than $42 million. And each year these companies will be entitled to claim, on the basis of such payment, a credit against their income tax liability (not merely

[4] Ontario, like Quebec, changed its income tax law in 1957 to make insurance companies subject to income taxes to the same extent as under Part I of the Dominion Income Tax Act (Fdg. 69, App. A, *infra*, p. 50).

a deduction from gross income) of some $5 million in the aggregate, if the ruling of the Court of Claims stands.

2. That ruling, we submit, rests on a misconception of the purpose and meaning of the "in lieu" provision of the foreign tax credit. This Court has never had occasion to construe that provision. We urge that it do so here in order to close a large loophole created by the ruling below.

a. Congress, in Section 131(h) of the Internal Revenue Code of 1939 (added by the Revenue Act of 1942, 56 Stat. 798) and Section 903 of the 1954 Code, did *not* provide that a company exempt from foreign income tax could credit any other tax it might happen to pay in the foreign jurisdiction. A tax, to be creditable, must be "in lieu of" an income tax "otherwise generally imposed." It must, in other words, be a specific substitute for a general income tax that would otherwise be applicable. The legislative history indicates that what Congress primarily had in mind were instances where administrative problems precluded taxing net income directly. Hearings on the Revenue Act of 1942 before the Senate Committee on Finance, 77th Cong., 2d Sess., pt. 1, pp. 207–208, 216–217; S. Rep. No. 1631, 77th Cong., 2d Sess., pp. 131–132;[5] see, also,

[5] The representative of the National Foreign Trade Council—the moving force behind the "in lieu" provision—gave the following example (Hearings, *supra*, p. 207):

> You can imagine yourself in the position of the tax administrator in Cuba, for example, who has there in Habana the branch of an enterprise manufacturing various articles in the United States, and selling them in Cuba. The Cuban tax administrator can easily verify

Treas. Reg. § 1.903–1 (App. B, *infra*, pp. 54–55). Congress consistently rejected broader proposed measures both before enactment of the Revenue Act of 1942 and in the intervening period before reenactment of the "in lieu" provision in the 1954 Code. (See Hearings on the Revenue Revision of 1950 before the House Committee on Ways and Means, 81st Cong., 2d Sess., pt. 1, pp. 605–607; Hearings on the Revenue Revision of 1951 before the House Committee on Ways and Means, 82d Cong., 1st Sess., pt. 1, p. 250; H. Rep. No. 1337, 83d Cong., 2d Sess., pp. 76–77, A250–A252; S. Rep. No. 1622, 83d Cong., 2d Sess., pp. 104–105.) And the term "in lieu of" is used throughout the Revenue Act of 1942 to indicate a substitution of one tax provision for another specific provision or tax that would otherwise be applicable. (See §§ 104, 105(b), 135, 136, 150(j), 165(c), 172, 185, 210(b), 213, 222, 303, 508).

It is thus plain that the only type of non-income tax embraced by the foreign tax credit is one specifically fashioned to take the place—to serve the function—of

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the gross income of that enterprise, but the Cuban tax administrator has no way of verifying the expenses, most of which are incurred in the United States and in transporting the goods to Cuba. So Cuba resorted to a very simple empirical method of taxation. It was first resorted to in connection with shipping enterprises. * * * They arbitrarily assumed that the expenses of the enterprise would be equal to about one-half of the gross income, but instead of reducing the gross income by one-half they simply cut the rate applicable to Cuban enterprises, namely, 6 percent to 3 percent, and provided in the income tax law that this rate be applied directly to the gross income of a foreign shipping company.

the general income tax. See *United States* v. *Waterman S. S. Corp.*, 330 F. 2d 128, 131 (C.A. 5), affirmed on another issue, 381 U.S. 252; *Commissioner* v. *American Metal Co.*, 221 F. 2d 134, 140 (C.A. 2), certiorari denied, 350 U.S. 829.

b. The Court of Claims impliedly rejected this fundamental precept in the instant case by viewing as irrelevant the persuasive indications that Canadian premiums taxes are not income tax substitutes. By focusing on the mere exemption from income tax, the court broadened the credit far beyond its intended scope.

(1) The premiums tax is an excise tax—a gross-receipts tax—and it is commonplace for firms to pay both excise and income taxes.[6] Excise taxes are typically in addition to, not in lieu of, income taxes. The Canadian premiums taxes, therefore, cannot realistically be presumed to be income tax substitutes without some clear indication that the legislature so intended. There was none here. Indeed, it is clear that

[6] Our Revenue Act of 1918, c. 18, 40 Stat. 1057, affords an illustration of the simultaneous imposition of income and premiums taxes on insurance companies. Except for certain small farmers' mutuals and the like (see 1918 Act, § 231(10), all insurance companies were then fully taxable on their underwriting income (profit from receipt of premiums in exchange for insurance) and investment income (profit from investing reserve funds held to meet policy obligations). 1918 Act §§ 230, 233. They were additionally subject to a 1 percent premiums tax or similar tax under Section 503 of the Act. Along with other corporations, moreover, insurance companies also paid a "special excise" on capital, surplus, and undivided profits. 1918 Act, § 1000 (a), (b), (c).

the provincial premiums taxes were, prior to the introduction of an income tax, substitutes for other *excise* taxes imposed generally on corporations, and they continue to be so.

(2) The Dominion imposes both premiums and income taxes on all domestic insurance companies save mutual insurance companies. Imposition of both taxes on the same companies is plainly inconsistent with the view that the premiums taxes are substitutes for income taxes. Were they such, it would be clearly inappropriate to subject the same company to both. We stress that foreign life insurance companies are exempt from Canadian income taxes for reasons unconnected with any notion that the premiums taxes they pay are in place of income taxes.

(3) The credit allowed under the Court of Claims' view thwarts the obvious purpose of the in-lieu provision of the foreign tax credit—equalizing the tax burdens of American businessmen within a foreign jurisdiction. Many American businesses in Canada pay both Canadian excise and Canadian income taxes. They cannot credit the excise taxes against their federal income tax liability. It is anomalous that a life insurance company should be able to do so because Canada exempted it from income taxes.

This last point is especially significant. One would expect a tax "in lieu" of an income tax to be a special levy to which only the exempt companies would be subject. But the premiums tax is a general tax imposed on insurance companies—those that pay, as well as those exempt from, income tax. It

is, in short, manifestly not an income tax substitute.

c. The Court of Claims' failure to weigh the foregoing points demonstrates, we submit, its tacit adoption of the view that all a taxpayer need show to credit a foreign excise tax is that he is exempt from the foreign jurisdiction's income tax. Indeed, solely on the basis of the provisions exempting insurance companies from various income taxes the court below concluded that the several legislatures had made "a deliberate choice between income and premiums taxes" which "is enough to characterize the premiums taxes as imposed 'in lieu of' income taxes." (App. A, *infra*, pp. 23–24.) We believe that this view is untenable and that it raises an issue warranting review by this Court.[7]

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[7] We point out that, unless review is granted by this Court, the ruling below will in all likelihood be final and conclusive on the question presented. No conflict among circuits is likely to develop, since any insurance company can bring a refund action in the Court of Claims, whose jurisdiction is nationwide. To be sure, an appeal raising a related question is now pending in the Ninth Circuit, *United States* v. *Occidental Life Insurance Co.*, No. 21039. However, that circuit has already held that Canadian premiums taxes are "in lieu of" income tax in the case of non-life mutual insurance companies. *Northwestern Mutual Fire Ass'n* v. *Commissioner*, 181 F. 2d 133.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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